



DEFENSE CONTRACT AUDIT AGENCY
DEPARTMENT OF DEFENSE
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IN REPLY REFER TO

PPS 730.5.26

June 27, 2014
14-PPS-012(R)

MEMORANDUM FOR REGIONAL DIRECTORS, DCAA
HEADS OF PRINCIPAL STAFF ELEMENTS, HQ, DCAA

SUBJECT: 14-PPS-012(R) Guidance on Establishing Provisional Billing Rates

Headquarters developed standard procedures for establishing provisional billing rates for auditors to use.

Why Did Policy Develop New Standard Procedures for Provisional Billing Rates?

Policy developed standard procedures for the 15500 activity code to establish provisional billing rates in accordance with the requirements of FAR 42.704. The FAR indicates whoever is responsible for establishing final indirect cost rates (auditor or contracting officer) also is responsible for establishing provisional billing rates. Provisional billing rates should be established early in the contractor's fiscal year. Auditors should use the new procedures to establish or assist the contracting officer in establishing provisional billing rates. Auditors may use the new procedures to adjust for significant billing rate changes throughout the year. We have included the new procedures as Enclosure 1 and will update APPS.

FAOs should begin using the new standard procedures for the provisional billing rates on October 1, 2014; however, earlier implementation is encouraged.

Questions and Further Information

FAO personnel should direct questions to their regional points-of-contact, and regional personnel with questions should contact Policy Publications and Systems Division at (703)767-3220 or by e-mail at DCAA-PPS@dcaa.mil.

/s/ Donald J. McKenzie
Assistant Director
Policy and Plans

Enclosures: 2

1. Standard Program for Establishing Provisional Billing Rates
2. Frequently Asked Questions

DISTRIBUTION: E

Activity Code 15500	Establishment of Provisional Billing Rates
Version 1.0 dated May 2014	
Purpose and Scope	
<p>1. The purpose of this assignment is to establish or adjust provisional billing rates as required by FAR 42.704, Billing Rates. The scope of the work performed in this assignment does not constitute an audit or attestation engagement under generally accepted government auditing standards (GAGAS).</p>	
<p>2. FAR 42.704(a) states that the person responsible for establishing final indirect cost rates (contracting officer or auditor) is also responsible for determining provisional billing rates.</p> <p>a. If the ACO is responsible for establishing the contractor's provisional billing rates and has established the rates, this assignment should not be opened. A copy of ACO's letter with established provisional billing rates should be placed in the Perm File and used for pre-payment reviews (voucher processing). In most cases, any support to the ACO in establishing provisional billing rates should be done as part of the audit team's normal interaction with the ACO and no assignment should be opened.</p> <p>b. If the ACO is responsible for establishing the contractor's provisional billing rates and has requested the auditor's assistance, use the procedures below and issue a memorandum with recommended provisional billing rates to the contracting officer, or if so desired by the ACO, a letter directly to the contractor establishing provisional billing rates on behalf of the ACO.</p> <p>c. If the auditor is responsible for establishing provisional billing rates, this assignment should result in a letter directly to the contractor, which specifies the approved provisional billing rates, with a copy to the ACO.</p>	
<p>3. Provisional billing rates should be established in a timely manner, typically at the beginning of a contractor fiscal year (i.e. to support the first voucher submitted for the year).</p> <p>a. Contractors should be encouraged to submit provisional billing rates at the end of the fiscal year to establish billing rates for the new fiscal year.</p> <p>b. If the contractor does not submit provisional billing rates, FAR 42.704 allows the contracting officer or auditor to establish rates considering historical unallowable, nonrecurring costs, and new or changed conditions.</p> <p><u>NOTE – In no case should the FAO delay establishing rates waiting for a contractor submission.</u></p>	
<p>4. Auditors may use this program to adjust established provisional billing rates during the contractor fiscal year if the contractor's indirect rates fluctuate significantly from the established provisional billing rates.</p>	
<p>5. Auditors may use this program to adjust established provisional billing rates if the contractor's rates in the final indirect cost rates proposal differ significantly from the established provisional billing rates.</p>	
<u>References</u>	
1. CAM 6-705.1 Provisional Billing Rates	
2. FAR 42.704 Billing Rates	

3. FAR 52.216-7 Allowable Cost and Payment	
C-01 Provisional Billing Rates	WP Reference
1. Notify the contractor you are initiating the process of establishing billing rates and ask if the contractor wishes to provide any input (e.g., budget, projections for changes, etc.) related to any anticipated changes in business volume, organizational structure, and/or indirect rate structure for the new fiscal year.	
2. Review the FAO perm files for relevant information which may impact provisional billing rates. <i>Note -- If no historical information is available, the auditor will need to obtain a forecast from the contractor to establish provisional billing rates. (This could be simply getting the proposal for the award of the contract and evaluating the proposed indirect cost rates)</i>	
3. Review incurred cost audit reports to ascertain the significance and trend of any questioned costs/rates. If significant questioned costs were identified, consider decrementing by a similar amount when establishing the provisional billing rates. <i>Note – The auditor should consider the relevance of questioned costs from prior years to determine if it is likely that questioned costs identified several years ago could impact the current billing rates.</i>	
4. Compare the billing rates from prior years to contractor actual year end rates. If there are significant variances, obtain an explanation from the contractor. <i>Note – The prior year actual rates do not have to be audited.</i>	
5. If applicable, compare the rates in the incurred cost proposal for the contractor’s prior fiscal year with established billing rates for current year. If there are significant variances, discuss with the contractor, and make any appropriate adjustments to the billing rates.	
6. If the contractor has submitted input (e.g., budget, projections for changes, etc.) for its new fiscal year, have the contractor provide a walk-through of the input and any significant changes from previous year’s rates.	
7. Summarize what the procedures above have disclosed and make any appropriate adjustments to the billing rates.	
8. Discuss the adjusted rates with the contractor.	
A-01 Concluding Steps	WP Reference
1. Summarize results.	

2. If the auditor is responsible for determining the provisional billing rates, issue a letter directly to the contractor, which specifies the approved billing rates, with a copy to the ACO.	
3. If the ACO is responsible for determining the provisional billing rates in accordance with FAR 42.704(a) and has requested the auditor's assistance, issue a memorandum with recommended billing rates to the ACO, or if so desired by the ACO, a letter directly to the contractor establishing billing rates on behalf of the ACO.	

FREQUENTLY ASKED QUESTIONS

Guidance on Establishing Provisional Billing Rates

Question 1. Is the contractor required to submit an indirect rate proposal or budget to establish provisional billing rates?

Answer. No. FAR 42.704 does not specifically require contractors to submit a billing rate proposal. We should encourage contractors to submit a billing rate proposal at the end of the fiscal year so that we can establish the rates early in the new fiscal year. The contractor is familiar with its indirect costs, business volume and changes in business conditions, and therefore, should be able to estimate provisional billing rates. However, the contractor's failure to submit a billing rate proposal or budget does not waive our responsibility of establishing the provisional billing rates. FAOs should not delay in establishing the provisional billing rates.

If the contractor does not provide a provisional billing rate proposal, the FAR requires the auditor or contracting officer to establish provisional billing rates in order to prevent significant over or underpayment. Absent a provisional billing rate proposal, billing rates may be established by considering historical data, unallowable costs, nonrecurring costs, and new or changed conditions.

Question 2. Why is it important to establish current provisional billing rates?

Answer. Contractors use provisional billing rates for interim reimbursement of indirect costs, which generally represent a significant portion of contract costs billed. In some cases, indirect cost rates can vary significantly due to changes in expenses or the allocation bases, or changes in the contractor's business conditions (e.g., new healthcare plan, gain or loss of a significant contract). Therefore, it is important to establish current billing rates which are as close as possible to the final indirect cost rates to prevent significant over or under billing. However, for many smaller contractors this is not the case and historical information is sufficient to establish provisional billing rates.